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No. 80-1614

In the Supreme Court of the United States

OCTOBER TERM, 1980

GEORGE F. JEWETT, JR.
and
LUCILLE M. JEWETT,
PETITIONERS,
v.
COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR PETITIONERS

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I

QUESTIONS PRESENTED FOR REVIEW

1. Is an unequivocal and effective disclaimer of a contingent remainder interest under a trust, made prior to the death of the life beneficiary, a taxable transfer for federal gift tax purposes?

2. Under Treasury Regulation §25.2511-1(c) does the "reasonable time" for disclaimer of a contingent remainder interest begin to run from the date of creation of the remainder interest or from the date of death of the life beneficiary?

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR PETITIONERS

The Petitioners George F. Jewett Jr. and Lucille M. Jewett respectfully pray that the judgment of the United States Court of Appeals for the Ninth Circuit entered in this proceeding on December 9, 1980 be reversed.

Opinions Below

The opinion of the United States Court of Appeals for the Ninth Circuit is reported at 638 F.2d 93 (9th Cir. 1980), 47 AFTR 2d 151, 212, and is reprinted at A-1 through A-6.[1] The

[1] References herein to the Joint Appendix are denoted "J.A. 1" and to documents included in the Appendix to the Petition for Certiorari "A-1".

opinion of the United States Tax Court is reported at 70 T.C. 430 (1978), CCH Tax Ct. Dec. ¶35,213 (1978), and is reprinted at A-7 through A-19, as amended by Order reprinted at A-23 through A-25.

Jurisdiction

The judgment of the United States Court of Appeals for the Ninth Circuit was rendered and entered on December 9, 1980. A petition for rehearing was denied by Order entered on February 18, 1981. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. §1254(1).

Statutes and Regulations

I.R.C. §2501. *Imposition of Tax.*

(a) *Taxable Transfers* —

(1) *General Rule.* — A tax, computed as provided in section 2502, is hereby imposed for each calendar quarter on the transfer of property by gift during such calendar quarter by any individual, resident or nonresident.

* * *

I.R.C. §2511. *Transfers in General.*

(a) *Scope.* — Subject to the limitations contained in this chapter, the tax imposed by section 2501 shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible; but in the case of a nonresident not a citizen of the United States, shall apply to a transfer only if the property is situated within the United States.

* * *

Treasury Regulation §25.2511-1(c), 26 C.F.R. 25.2511(c): The text of 26 C.F.R. §25.2511-1(c) is set forth at A-30 - A-31.

Statement of the Case

1. *Statement of Facts*

Margaret W. Jewett (hereinafter "the Testatrix") died on January 14, 1939, leaving a will which created a trust for the benefit of her husband during his lifetime and thereafter for the benefit of her son and daughter-in-law (George F. Jewett, Jr.'s parents) during their lifetimes (A-21). On the death of their survivor, the will directs distribution of the remainder to her son's then-living children. The share of any then-deceased child is to be distributed directly to his issue.

The Testator's husband and son died prior to 1972. (A.-21) The remaining life beneficiary, George F. Jewett, Jr.'s mother, is still living. (A-21)

Under the trust, George F. Jewett, Jr. (hereinafter "Jewett"), would become entitled to a share of the trust remainder only if he survives his mother. (A-21)

In 1972, while his mother was still alive, Jewett executed disclaimers of his contingent remainder interest in the trust. (A-21-A-22) Those disclaimers were unequivocal and effective under the governing state law (Massachusetts). (A-3)

Jewett and his wife disclosed the disclaimers on their 1972 United States Gift Tax Returns, but did not report them as taxable transfers for federal gift tax purposes. (A-10)

In February 1976, the Internal Revenue Service issued Notices of Deficiency asserting that the disclaimers were taxable transfers. (See A-10-A-11)

2. *Proceedings Below*

On May 5, 1976, petitioners filed a Petition in the United States Tax Court for the redetermination of the deficiencies determined by the I.R.S. (J.A. 1). Jurisdiction in the Tax Court existed pursuant to 26 U.S.C. §7442 and §6213. That Petition alleged that the Notices of Deficiency erroneously determined that the disclaimers were taxable transfers for federal gift tax purposes.

On June 13, 1978, the Tax Court filed an Opinion (A-7) holding that Jewett's disclaimers were taxable transfers for federal gift tax purposes. It was undisputed that the law of Massachusetts governs the validity and effectiveness of Jewett's disclaimers. (A-2, A-3). The Tax Court conceded that the disclaimers were unequivocal and effective under Massachusetts law (A-12), but asserted that they were not timely under Treasury Regulation §25.2511-1(c), because the "reasonable time" provision of that Regulation must be measured from the date of death of the Testatrix (in 1939) rather than from the date of death of the life beneficiary (who is still living) (A-14, A-15).

Petitioners filed a Motion for Reconsideration, which was denied on July 19, 1978 (A-26). Also on July 19, 1978, the Tax Court issued an Order amending its July 13, 1978 Opinion in certain respects, without changing the result (A-23).

On August 17, 1978, Decision was entered by the Tax Court in accordance with its Opinion of June 13, 1978, as amended (A-27).

On November 13, 1978, Appellants filed their Notice of Appeal to the Court of Appeals for the Ninth Circuit.

In an Opinion filed on December 9, 1980, from which one Judge dissented (A-6), the Court of Appeals for the Ninth Circuit affirmed the decision of the Tax Court (A-1), stating that a disclaimer of a contingent remainder interest must be made

within a reasonable time after knowledge of the transfer to the disclaimant. It held that the relevant "transfer" was the creation of the contingent remainder interest (by the death of the Testatrix 33 years before) rather than the possible transfer of the trust property to Jewett upon the death of the life beneficiary (which event had not, and still has not, occurred). In so holding, the Opinion expressly disagreed with the decision of the United States Court of Appeals for the Eighth Circuit in *Keinath* v. *Commissioner*, 480 F.2d 57 (8th Cir. 1973). (A-4).

On December 19, 1980, petitioners filed a motion for rehearing and suggestion for rehearing *en banc*. That motion was denied on February 18, 1981. (A-29)

Petitioners filed a Petition for Certiorari to this Court on March 25, 1981, and Certiorari was granted on June 1, 1981.

Summary of Argument

A disclaimer is fundamentally different from a voluntary transfer. Treasury Regulation §25.2511-1(c) recognizes this fundamental difference. State law, both decisional and statutory, uniformly holds a renunciation of a contingent remainder interest while the life beneficiary is still alive to be a timely disclaimer, not a voluntary transfer. Treasury Regulation §25.2511-1(c) was intended to codify that common law principle, and its language is consistent with that rule.

The interpretation of Treasury Regulation §25.2511-1(c) urged by the Commissioner and adopted by the Ninth Circuit, that such a timely disclaimer constitutes a voluntary transfer for federal gift tax purposes, is incorrect. It is contrary to the language of the Regulation, it is inconsistent with tax laws intended to complement the gift tax, and it is fundamentally unfair. The position of the Commissioner should therefore be rejected and the decision of the Ninth Circuit herein should be reversed.

Argument

A. A Disclaimer Is A Refusal To Accept Ownership Of Property Rather Than A Transfer Of Property By The Disclaimant.

The federal gift tax is imposed upon "the transfer of property by gift". Internal Revenue Code §2501, 26 U.S.C. §2501. The sole issue before this Court is whether the disclaimer of a contingent remainder interest, made while that interest is still contingent, constitutes a taxable transfer for federal gift tax purposes. Analysis of that issue must start with an understanding of the nature of a disclaimer and how it differs from a voluntary transfer.

A disclaimer is a refusal to accept property *ab initio*. *Bel* v. *United States*, 452 F.2d 683, 693 (5th Cir. 1971); *City National Bank & Trust Co.* v. *United States*, 203 F. Supp. 398, 402 (S.D. Ohio 1962) aff'd, 312 F.2d 118 (6th Cir. 1963), *cert. denied*, 373 U.S. 949 (1963).[2] The law of disclaimer is founded on the basic property law doctrine that a transfer is not complete until acceptance by the recipient, and that no person can be forced to accept property against his will. *See Foley* v. *Allen*, 170 F.2d 434, 437 (5th Cir. 1948); 38 C.J.S., *Gifts* §29; Scott, *Trusts*, §36.1 (3rd Ed. 1967). If the potential recipient disclaims property before its transfer to him, that transfer is ineffective, the property never vests in the potential recipient, and disposition of the disclaimed property proceeds as if the disclaimant had never had any potential rights in the property.

[2] See also H.R. Rep. No. 94-658, 94th Cong., 2d Sess., reprinted in 1976 *U.S. Code Cong. & Ad. News*, Vol. 4, 2897, 3419 (disclaimer defined as a "refusal to accept the ownership of property or rights with respect to property"), and S. Rep. No. 1599, 89th Cong. 2d Sess. (1966), 1966-2 C.B. 798, 801 (disclaimer defined as "a complete and unqualified refusal to accept some or all of the rights to which one is entitled").

A fundamental distinction between a disclaimer and a voluntary transfer is that in a voluntary transfer the transferor selects the recipients of the property, while in a disclaimer the disclaimant can make no such selection. *See Keinath* v. *Commissioner, supra,* 480 F.2d at 65. When a contingent beneficiary under a trust disclaims his interest in the trust, as in this case, the disposition of the disclaimed property is determined by the instrument creating the trust and the applicable state law. *Id.* It is *not* determined by the terms of the disclaimer itself.

In the instant case, the persons who will become entitled to the disclaimed property on the death of the life beneficiary are determined by the will of the Testatrix, and are *not* determined by the terms of Jewett's disclaimers.[3] Jewett's disclaimers merely renounced any future right to receive the corpus of the trust; they did not, and as disclaimers *could* not, purport to direct that future distribution.

The federal tax laws have long recognized that the effect of a disclaimer is to allow property to pass directly from the original owner to the party or parties taking as a result of the disclaimer, rather than from the disclaimant to those parties. Thus, Section 812(d) of the Internal Revenue Code of 1939 treated amounts passing to charity as a result of disclaimer by an estate beneficiary as having passed directly from the dece-

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[3] In fact, the identity of the ultimate recipients cannot even now be determined. Under Massachusetts law, it is likely (although not certain), that the share to which Jewett would have been entitled, had he survived the life beneficiary without disclaiming, will be distributed to Jewett's issue (if any) living on the death of the life beneficiary, in shares determined by right of representation (i.e., according to the provisions of the will as if Jewett had predeceased the life beneficiary). See Mass. Gen. Laws c. 191A, §7. Of course, at this time (and *a fortiori* at the time of the disclaimers) it is impossible to determine who those persons will be or indeed whether *any* persons within that class will survive the life beneficiary.

dent to the charity, so that an estate tax charitable deduction was allowed for

> "[t]he amount of all [charitable] bequests, legacies, devises or transfers (including the interest which falls into any such bequest, legacy, devise or transfer as a result of an irrevocable disclaimer of a bequest, legacy, devise, transfer, or power, if the disclaimer is made prior to the date prescribed for the filing of the estate tax return . . . .)."

26 USC §812 (1939) (carried over as Section 2055(a) of the Internal Revenue Code of 1954).

Conversely, Section 812(e)(4)(A) of the 1939 Code denied the federal estate tax marital deduction for amounts passing to third parties as a result of disclaimer by a decedent's surviving spouse, treating such amounts as having passed directly from the decedent to those parties. This provision was subsequently incorporated in Section 2056(d)(1), the successor provision of the 1954 Code.

Treasury Regulation §25.2511-1(c), at issue herein, recognizes the fundamental difference between a refusal to accept property *ab initio* and the disposition of property already owned:

> "(c) . . . . Where the law governing the administration of the decedent's estate gives a beneficiary . . . a right to completely and unqualifiedly refuse to accept ownership of property transferred from a decedent . . . a refusal to accept ownership does not constitute the making of a gift if the refusal is made within a reasonable time after knowledge of the existence of the transfer. The refusal must be unequivocable [sic] and effective under the local law. There can be no refusal of ownership of property after its acceptance . . . . In the absence of facts to the contrary, if a person fails to accept a transfer to him of ownership of a decedent's property within a reasonable time after learning of the existence of the transfer, he will be presumed to have accepted the property . . . ."

The central issue in this case is whether the computation of the "reasonable time" allowed by the Regulation runs from the establishment of a trust identifying the taxpayer as having a contingent remainder interest, or from the death of the life beneficiary, when ownership of the trust property passes to the taxpayer.

Two United States Courts of Appeals have addressed that question: the Ninth Circuit in the instant case and the Eighth Circuit in *Keinath* v. *Commissioner*, 480 F.2d 57 (8th Cir. 1973), followed in *Cottrell* v. *Commissioner*, 628 F.2d 1127 (8th Cir. 1980) (*en banc*).

B. In Contrast With The Decision Below, The Decision Of The United States Court Of Appeals For The Eighth Circuit In *Keinath* v. *Commissioner* Was Well-Reasoned And Correct.

1. *The Opinion Below Lacked A Reasoned Basis.*

The Opinion below directly and expressly created a conflict with the only other Circuit Court of Appeals authority in point, the decision of the Eighth Circuit in *Keinath* v. *Commissioner*, 480 F.2d 57 (8th Cir. 1973), which was recently followed by that Circuit, sitting *en banc*, in *Cottrell* v. *Commissioner*, 628 F.2d 1127 (8th Cir. 1980). In those decisions the Eighth Circuit had held that the "reasonable time" provision of Treasury Regulation §25.2511-1(c) must be computed from the date of the death of the life beneficiary, not the date of the establishment of the trust identifying the taxpayer as having a contingent remainder interest.

The Ninth Circuit's opinion, in rejecting the *Keinath* rule, is sparse in its reasoning. In essence, it discussed *Keinath*, stated: "We must respectfully disagree", and without further explanation held that the timeliness of the disclaimer for federal tax purposes was measured from the creation of the trust rather than from the death of the life beneficiary. (A-4, A-5.)

To the extent a rationale appears for this ruling, it seems to have been somewhat as follows:

1. A contingent remainder interest is "property", the voluntary transfer of which by Jewett would be subject to the gift tax. (A-2)

2. The federal standard of timeliness is imposed over and above state law requirements. (A-5)

3. Under federal law, the disclaimer by Jewett had to be made within a reasonable time after the "transfer" (actually, the creation) of the contingent remainder interest to him. (A-5)

Points 1 and 2 may be correct. However, they do not logically compel the conclusion in point 3. In fact, the Ninth Circuit's opinion offers no explanation whatsoever of the rationale for the holding in point 3.

2. *The Eighth Circuit had a Reasoned Basis for the Keinath Decision.*

Had this case arisen in the Eighth Circuit, *Keinath* v. *Commissioner*, 480 F.2d 57 (8th Cir. 1973), would have been directly controlling and dispositive. In *Keinath*, as in the instant case, a testamentary trust provided income to a life beneficiary (the testator's widow), and upon her death the remainder was to be distributed outright to the testator's sons, with the share of any then-deceased son to be distributed to that son's issue. As in the instant case, the designated remaindermen (the testator's sons) would take nothing if they did not survive the life beneficiary.

Less than six months after the death of the life beneficiary, but nineteen years after the death of the testator, one of the sons filed a disclaimer of his interest. In *Keinath*, as in the instant case, the issue was squarely presented as to whether the disclaimer was executed within a "reasonable time" under Treasury Regulation §25.2511-1(c).

The Eighth Circuit recognized that there is no definition in the Internal Revenue Code or Treasury Regulations, or anywhere else in the federal law, of the term "reasonable time" or of the starting point for the computation of a "reasonable time." However, the Eighth Circuit properly recognized that Treasury Regulation §25.2511-1(c) was "a codification of common law principles applicable to the doctrine of disclaimers," 480 F.2d at 61, and stated:

> "In determining 'reasonable time' and the related issue of when the reasonable time period commences, we perforce, absent a federal statute or regulation defining reasonable time, must look to the law of the states. We are not conclusively bound by the state law, but this is the only field to probe for legal decisions and discussions on the phrase 'reasonable time' as used in the context of making valid disclaimers." *Id.* at 61-2. (Footnote omitted)

The Eighth Circuit found the state law precedents to be unanimous:

> "The appellants maintain, without any refutation by the Commissioner, that all of the authorities who have considered this question have concluded that the time in which a remainder interest subject to divestiture must be disclaimed commences upon the death of the life beneficiary. . . . We have found no contrary authority and think that this is the prevailing common law rule. . . ." 480 F.2d at 64.

Having reviewed the relevant state decisional law, the Eighth Circuit concluded that:

> ". . . the holder of a vested remainder interest subject to divestiture has a reasonable time within which to renounce or disclaim the remainder interest after the death of the life beneficiary and that an unequivocal disclaimer filed within six months thereof is made within a reasonable time." 480 F.2d at 64.

The Eighth Circuit found this rule to be "sound in principle and reason," because:

> "A remainder subject to divestment does not convey or transfer any actual control or current beneficial interest in property to the remainderman .... In the instant case the remainderman Cargill had really nothing to accept or renounce by way of beneficial ownership or control of the property until he succeeded in outliving the life beneficiary." *id.*

Its conclusion was therefore consistent with the leading cases of *Corliss* v. *Bowers*, 281 U.S. 376 (1930) and *Estate of Sanford* v. *Commissioner*, 308 U.S. 39 (1939), which set forth the principle that "taxation is not so much concerned with the refinements of title as it is with the actual command over the property taxed," 281 U.S. at 378, 308 U.S. at 43.

The *Keinath* rule thus represents a reasoned, principled and persuasive interpretation of the Regulation, and as such it stands in sharp contrast with the decision of the Ninth Circuit in this case.

C. Treasury Regulation §25.2511-1(c) Is A Codification Of The Common Law Of Disclaimer.

The Eighth Circuit in *Keinath* considered Treasury Regulation §25.2511-1(c) to be "a codification of the common law principles applicable to the doctrine of disclaimers," 480 F.2d at 61. That reading was consistent with the regulatory language and the existing law at the time the Regulation was adopted. The Regulation was intended to codify and clarify the common law, not to change it.

Treasury Regulation §25.2511-1 was first published, in proposed form, on January 3, 1957. At that time the leading case on the federal tax impact of disclaimers was *Brown* v. *Routzahn*, 63 F.2d 914 (6th Cir. 1933), *cert. denied*, 290 U.S. 641

(1933), which established the thereafter universally accepted rule that a disclaimer which is effective and timely under the governing state law is not a taxable transfer for federal tax purposes. *Commissioner* v. *Vease's Estate*, 314 F.2d 79, 88 (9th Cir. 1963).

Brown involved a disclaimer by a husband, shortly before his death, of a bequest made to him by his predeceased wife. The Commissioner contended that the disclaimer was a transfer in contemplation of death for purposes of the federal estate tax. Under state law the husband was entitled to disclaim his interest in his wife's estate at any time prior to actual distribution of the estate by the testamentary trustees, and that distribution did not take place until after the disclaimer, some eight years after the wife's death. The United States Court of Appeals for the Sixth Circuit held that since the disclaimer was effective and timely under state law, the transfer of property from the wife to the husband was never completed, and accordingly there could be no subsequent transfer by him in contemplation of death. Refusal to accept a gift of property was not a transfer of an interest in the property.

Brown v. *Routzahn* was recognized as establishing that:

> "... the federal tax on transfers ... is levied on the transfer of property; not on the exercise of a right to renounce testamentary gifts. Accordingly, if under local law a legatee or devisee has the option of accepting or rejecting his testator's bounty, rejection of the gift does not result in a taxable transfer to its residuary recipient."

Commissioner v. *Vease's Estate*, 314 F.2d 79, 88 (9th Cir. 1963).

The logical corollary to *Brown* v. *Routzahn*, under the common law of disclaimer extant at the time the Regulation was promulgated, was *Hardenbergh* v. *Commissioner*, 198 F.2d

63 (8th Cir. 1952), *cert. denied*, 344 U.S. 836 (1952), where under local law the disclaimant had *no* option of accepting or rejecting a decedent's bounty. In *Hardenbergh*, the taxpayers' father died intestate, and under state law, ownership of the decedent's estate vested automatically and immediately in the taxpayers and a third heir, without any need for acceptance or option of rejection by the recipient, subject only to a qualified vesting of legal title in the administrator of the estate solely for purposes of administration. The taxpayers renounced their interest in the estate, but the court held that since under state law title had already vested in the taxpayers the renunciation was a taxable transfer of the taxpayers' property to the non-disclaiming heir.

Treasury Regulation §25.2511-1(c), as originally published in proposed form on January 3, 1957, was an attempt to restate the common law of disclaimer as expressed in *Brown* and *Hardenbergh*. The proposed Regulation provided:

> "... *The renunciation of a vested property interest*, such as the interest of an heir or next-of-kin, or devisee in whom title immediately vests upon a decedent's death under local law, *constitutes a gift* to those persons who receive the property interest by means of the renunciation. *On the other hand the renunciation* of a gift, bequest or inheritance, *if under local law title does not immediately vest, is not a gift* if the renunciation is complete, and is made within a reasonable time after knowledge of the existence of the interest. The renunciation must be unequivocal and effective under local law. A renunciation is a complete and unqualified refusal to accept the property to which one is entitled. There can be no renunciation of property after its acceptance ...." (Emphasis added)

22 Fed. Reg. at 58 (1/3/57).

The adoption of the "vested property interest" language, the specific mention of "the interest of an heir or next of kin" and the concept of immediate vesting of title defeating a disclaimer were manifestly taken from *Hardenbergh*. *See* 198 F.2d at 66.

In the final version of the Regulation, published on November 15, 1958, the language was changed somewhat, but the intent to adopt the common law of disclaimer was still clear:

> "(c) .... *Where the law governing the administration of the decedent's estate gives a beneficiary, heir, or next-of-kin a right to completely and unqualifiedly refuse to accept ownership of property transferred from a decedent* (whether the transfer is effected by the decedent's will or by the law of descent and distribution of intestate property), *a refusal to accept ownership does not constitute the making of a gift* if the refusal is made within a reasonable time after knowledge of the existence of the transfer. The refusal must be unequivocable [sic] and effective under the local law. There can be no refusal of ownership of property after its acceptance. Where the local law does not permit such a refusal, any disposition by the beneficiary, heir or next-of-kin whereby ownership is transferred gratuitously to another constitutes the making of a gift by the beneficiary, heir, or next-of-kin ...." (Emphasis added)

23 Fed. Reg. at 8910 (11/15/58).

The change in language from "renunciation of a vested property interest" to "refus[al] to accept ownership of property transferred from a decedent" appears to have been a deliberate effort to harmonize the *Hardenbergh* "vesting" language with the general common law principles stated in *Brown* v. *Routzahn*, while continuing to leave to state law the definition of those rights which are subject to disclaimer.

The language of the proposed Regulation, "within a reasonable time after knowledge of the existence of the *interest*" (emphasis supplied), might have supported the Ninth Circuit's view. In that sentence and in context the word "interest" could only have referred to some form of property interest *other than a vested property interest*, and it might well have encompassed a contingent remainder interest. However, in the Regulation as promulgated, the word "interest" has been changed to "transfer," a word used throughout the Regulation to mean the passing of "ownership of property" from the decedent. That change, which must be considered to have been deliberate, brought the Regulation into conformity with preexisting law by allowing a disclaimer upon the actual transfer of ownership to the disclaimant, rather than when the disclaimant was given only an "interest" in the decedent's property.

D. The Regulation Should Be Interpreted To Harmonize With Unanimous State Law Authority In Support Of The *Keinath* Rule.

In reaching its decision in *Keinath* the Eighth Circuit carefully reviewed the applicable state law, and found that "*all of the authorities* who have considered this question have concluded that the time in which a remainder interest subject to divestiture must be disclaimed commences upon the death of the life beneficiary . . . We have found *no contrary authority*." (emphasis supplied) 480 F.2d at 64.

Like the Eighth Circuit, the petitioners have been unable to find any "contrary authority." The statutes of at least 34 states expressly provide that disclaimers of contingent remainder interests can be made before the expiration of a certain period of time (generally six or nine months) after the death of the life

beneficiary.[4] Other states have adopted the same principle in decisional law. E.g., *Coleman* v. *Burns*, 103 N.H. 313, 171 A.2d 33 (1961) (New Hampshire). Page, Law of Wills, §49.8 (Bowe-Parker ed. 1962)

The Uniform Probate Code (1969), which has been adopted (as of January, 1981) in 14 states, specifically provides in §2-801(b)(2) (5th ed. Official 1977 Text):

> "An instrument renouncing a future interest may be filed not later than [9] months after the event determining that the taker of the property or interest is finally ascertained and his interest is indefeasibly vested."

Similarly, the Uniform Disclaimer of Transfers by Will, Intestacy or Appointment Act (1973), which has been adopted (as of January, 1981) in six states, provides in §2(b):

> "An instrument disclaiming a future interest shall be filed not later than [six] months after the event that determines that the taker of the property or interest is finally ascertained and his interest indefeasibly vested."

The Ninth Circuit's assertion that the timeliness of a remainderman's disclaimer must be measured from the creation of the remainder interest rather than from the death of the life beneficiary finds no support in state law or in the law of other

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[4] See statutes cited at A-32, plus:
Connecticut: Conn. Gen. Stat. Ann. §45-307 (West Supp. 1978) (nontestamentary gifts).
Maryland: Md. Est. & Trusts Code Ann. §9-202 (Supp. 1978).
Michigan: Mich. Stat. Ann. §§26.1236(2) & (12) (Supp. 1978).
New York: N.Y. Est., Powers & Trusts Law §2-1.11(a) (McKinney Supp. 1978).
Oklahoma: Okla. Stat. Ann. Tit. 84, §24 (West Supp. 1978).
Rhode Island: R.I. Gen. Laws §34-5-5-8 (1970).
Tennessee: Tenn. Code Ann. §31-103 (Supp. 1979).

Circuits, and the Ninth Circuit Opinion did not cite a single case, statute or secondary authority to support its conclusion. (A-4, A-5)

Until the decision below, persons contemplating a disclaimer of a contingent remainder interest could reasonably wait until the death of the life beneficiary before deciding whether to disclaim. No federal statute or regulation expressly conflicted with that principle,[5] and until 1978 the only decision of the Tax Court to the contrary had been reversed on that precise issue by the Eighth Circuit in *Keinath* v. *Commissioner, supra*, rev'g 58 T.C. 352 (1972).

The Ninth Circuit has judicially created a rule so removed from state law that Jewett, who justifiably believed that his disclaimer would not be a taxable gift, and who had not even reached the point at which a decision whether to disclaim had to be made, belatedly discovers that his disclaimer should have been made more than thirty years earlier (at the Testatrix's death in 1939), and in fact twenty years before the 1958 promulgation of Treasury Regulation §25.2511-1(c).

This Court should act to prevent the judicial creation of such a paradoxical and inequitable result, and to avoid such an unnecessary conflict between federal and state law concepts. Whenever possible the federal tax laws should be interpreted to be consistent with state law principles. *In re Nissen's Estate*, 345 F.2d 230, 234 (4th Cir. 1965) (terminology of Internal Revenue Code is to be "generally read and construed with reference to the law of the particular state"). *See Poe* v. *Seaborn*, 282 U.S. 101, 109-10 (1930) (federal income tax law must be applied consistently with the state community property law. Moreover, the regulatory background indicates that this

[5] The Tax Reform Act of 1976, P.L. 94-455, §2009(e)(2), did effect a material change as to contingent remainder interests created after 1976, as discussed *post* at 24.

Regulation was not intended to impose a fundamental conflict with state law, and it should be interpreted accordingly.

E. The Commissioner's Interpretation Of Treasury Regulation §25.2511-1(a) Is Inconsistent With The Plain Meaning Of The Regulatory Language.

Treasury Regulation 25.2511-1(c) requires that a disclaimer be made "within a reasonable time after knowledge of the existence of the transfer." The words "the transfer" refer back to the language of the first clause of the same sentence: "Where the law governing the administration of the decedent's estate gives a beneficiary . . . a right to . . . refuse to accept *ownership of property transferred from a decedent* . . ." (Emphasis added). Later in the regulation this "transfer" is similarly referred to as "a transfer . . . of *ownership of the decedent's property*." (Emphasis added).

Giving those words their ordinary meaning, the term "ownership of the decedent's property" at the very least must include outright ownership. In the instant case, Jewett cannot receive outright ownership of the Testatrix's property until the death of his mother. No "transfer" of such ownership to Jewett takes place until and unless he survives his mother. According the regulatory language its plain meaning he then would have a reasonable time after the "transfer" occasioned by his mother's death in which to disclaim ownership of the Testatrix's property, without fear that his refusal to accept outright ownership would constitute a gift to the residuary beneficiaries.

The Commissioner contends, however, that the right to disclaim is not so straightforward. He contends that as soon as Jewett received *any* interest in the decedent's property, including a contingent remainder interest — one which is fixed neither in quality nor in quantity and which may result in Jewett receiving nothing — he received "ownership of the

decedent's property." Therefore, in the Commissioner's view, if Jewett later were to receive outright ownership of the decedent's property, it would be too late to disclaim despite the plain language of the Regulation.

As Justice Frankfurter noted, when interpreting a statute the starting point is the statutory language itself. F. Frankfurter, Some Reflections on the Reading of Statutes, 47 Colum. L. Rev. 527, 535 (1947). Regulations, moreover, because they particularize, are not as generously or expansively interpreted as statutes. *Tobin* v. *Edward S. Wagner Co.*, 187 F.2d 977, 979 (2nd Cir. 1951). The Commissioner's interpretation that the transfer of "ownership" means something inconsistent with the transfer of outright ownership should be rejected.

F. Imposition Of A Gift Tax On Jewett's Disclaimers Contravenes The Congressional Intent That The Gift Tax Law Complement The Estate Tax.

In interpreting a regulation which is not clear on its face, federal courts should look to the intent behind the statute the regulation is purporting to enforce. *Trustees of Indiana University* v. *United States*, 618 F.2d 736, 739 (Ct. Cl. 1980). "... [A] regulation must be interpreted so as to harmonize with ... and not to conflict with the objectives of the statute it implements." *Id. See United Telecommunications, Inc.* v. *Commissioner*, 589 F.2d 1383, 1390 (10th Cir. 1978), *cert. denied*, 442 U.S. 917 (1979); *Usery* v. *Kennecott Copper Corp.*, 577 F.2d 1113, 1118 (10th Cir. 1977).

The gift tax was originally adopted as a "corollary" to or as "supplemental" to the estate tax. 65 Cong. Rec. 3119, 3120, 3122, 3172, 8095, 8096 (1924). The purpose of its enactment was "to prevent or compensate for avoidance of death taxes by taxing the gifts of property inter-vivos which, but for the gifts, would be subject ... to the tax laid upon transfers at death." *Estate of Sanford* v. *Commissioner*, 308 U.S. 39, 44 (1939). The intent of Congress was to achieve a "unified scheme of taxation of gifts whether made inter-vivos or at death." *Id.* at

48; R. Paul, *Federal Estate and Gift Taxation*, §15.04 (1942). The reports of both the House and Ways and Means Committee and the Senate Finance Committee on the 1932 gift tax statute emphasize that the gift tax was designed:

> to impose a tax which measurably approaches the estate tax which would have been payable on the donor's death had the gifts not been made and the property given had constituted his estate at his death. The tax will reach gifts not reached, for one reason or another, by the estate tax.

H.R. Rep. No. 708, 72d Cong., 1st Sess., 28 (1932); S. Rep. No. 655, 72d Cong., 1st Sess. (1932), 40.

The federal gift tax and the federal estate tax "are *in pari materia* and must be construed together." *Estate of Sanford* v. *Commissioner*, 308 U.S. 39, 44 (1939). The federal gift tax, I.R.C. §2501, taxes "the transfer of property by gift"; the federal estate tax, I.R.C. §2033, taxes "all property to the extent of the interest therein of the decedent at the time of his death." If the taxpayer does not transfer property during his lifetime, that "property" will remain in his estate, and be subject to the federal estate tax at his death.

It is well settled that a contingent remainder interest is not "property" includable in the remainderman's gross estate if he dies prior to the life beneficiary. *Estate of Williams* v. *Commissioner*, 62 T.C. 400 (1974). *See also Lee* v. *United States*, 63-1 USTC Para. 12,128 (S.D. Tex. 1962).[*]

If Jewett had predeceased his mother, therefore, the Testatrix's property would not have been subject to federal estate tax as part of his estate because her property would never have come into his estate. Similarly, as a result of Jewett's disclaimers

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[*] Conversely, a vested remainder interest (not subject to divestment, i.e., where the remainderman's estate will become entitled to it if he dies before it becomes possessory) *is* considered "property" includable in the remainderman's gross estate for federal estate tax purposes. *Dauphin Deposit Trust Co.* v. *McGinnes*, 324 F.2d 458 (3d Cir. 1963); *Estate of Hamilton* v. *Commissioner*, 35 T.C.M. 1609 (1976), *aff'd*, 3d Cir., April 12, 1978 (unpublished opinion), Fed. Est. & Gift Tax Rep. (CCH) Para. 19,013.

the Testatrix's property will never come into Jewett's estate. In either situation the terms of the Testatrix's will provide that her property will pass to others. Yet the Commissioner would impose a gift tax on that property in the one instance (disclaimer) while no estate tax would be imposed in the other (Jewett's death). Instead of creating "a unified system of taxation," which Congress intended, the Commissioner would apply the gift tax inconsistently with the estate tax, creating confusion and disharmony between the two taxes.

Similarly, imposition of the gift tax because of Jewett's disclaimers would be inconsistent with the specific treatment of analogous transactions under the estate and gift tax statutes. For example, the passage of property as the result of a disclaimer might be compared with the transfer of property pursuant to the exercise of a limited power of appointment. The holder of a limited power of appointment has broad control over the disposition of the appointive property, since he has the ability to select the recipients of property (though only among a specified class of donees). However, a disclaimant has no such control over the disposition of the disclaimed property. Rather, the disposition is controlled by the original instrument. The exercise (or non-exercise) of a limited power of appointment is not considered a taxable transfer, I.R.C. §2514, nor is property subject to a limited power of appointment includible in a decedent's gross estate, I.R.C. §2041, because the holder of the power does not have sufficient control over the appointive property. *A fortiori*, a disclaimer, involving a lesser degree of control, should not be considered a taxable transfer.

Indeed, the Commissioner has himself relied on the same distinction between a disclaimer, after which the property passes to others independent of any control by the disclaimant, and a transfer, in which the transferor exercises control over who receives the property. In Revenue Ruling 76-156, 1976-1 C.B. 292, a decedent's will provided:

> "In the event that any of my issue renounce his or her interest in my estate arising under this clause, such issue shall have the right to appoint all or any part of such interest, subject to any conditions, trusts and restrictions as such renouncing issue may determine, to any of my issue and the spouses of any of my issue."

One of the decedent's children renounced his bequest and appointed his share to persons other than those who would have taken under the will and governing state law had the disclaimer not been coupled with the exercise of the power of appointment. The IRS held that the disclaimer, because it was coupled with the exercise of the power of appointment, constituted a taxable gift by the decedent's child, because the child "has availed himself . . . of a positive opportunity to personally direct the ultimate disposition of the property in which [he] supposedly has renounced the ownership interest" and has "caused the property to be disposed of in a manner that was not specifically ascertainable from the terms of the decedent's will." Id. at 293.

To impose a gift tax on a transaction in which the disclaimant exercises less dominion or control over the property than a person who exercises a tax-free limited power of appointment is both inconsistent and fundamentally unfair.[7]

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[7] Unlike property subject to a limited power of appointment, property subject to a general power of appointment is included in a decedent's gross estate for federal estate tax purposes, and its exercise is a taxable transfer for federal gift tax purposes. I.R.C. §§2041, 2514. As with other areas of the federal tax law, the critical factor in the distinction between a general power of appointment and a limited power is the degree of control the taxpayer has over the disposition of the property:

> A person having a general power of appointment is, with respect to disposition of the property at his death, in a position not unlike that of its owner. The possessor of the power has *full authority to dispose* of the property at his death, and there seems to be no reason why the privilege which he exercises should not be taxed in the same degree as other property over which he exercises the same authority. (Emphasis added.)

G. The Ninth Circuit Decision Would Give Impermissible Retroactive Effect To A Statute Which Congress Intended To Be Prospective Only.

Under the Tax Reform Act of 1976, P.L. 94-455, 90 Stat. 1520, Congress added Section 2518 to the Internal Revenue Code, which dealt specifically with the question of the timeliness of disclaimers.

However, that new section is effective only as to interests created after December 31, 1976. P.L. 94-455, sec. 2009(e)(2), 90 Stat. at 1896. The House Report clearly recognized that, "In the case of transfers made before January 1, 1977, the rules relating to disclaimers under present [i.e., prior] law, including the period within which a disclaimer must be made, are to continue to apply ...." H.R. Rep. No. 94-1380, 94th Cong., 2d Sess., 66, reprinted in 1976 U.S. *Code Cong. & Ad. News*, vol. 4, 3431-3422. Furthermore, the House Report recognized *Keinath* as an accurate statement of the pre-existing law, *id.* at 3420, and in addition recognized that under the pre-existing law

> the Federal tax consequences of a disclaimer will largely depend upon its treatment under local law, i.e., its treatment as a disclaimer so that the person disclaiming is not considered to have held title to the property at any time. *Id.* at 3420.

H.R. Rep. No. 767, 65th Cong. 2d Sess. (1918), reprinted in 1939-1 C.B. 86, 101.

As Chief Judge Kaufman noted in *Estate of Rolin* v. *Commissioner*, 588 F.2d 368, 370 (2d Cir. 1978), the clear congressional purpose in enacting §2041 of the Internal Revenue Code (taxing general powers of appointment), and its predecessors, was "merely to ensure that since the possessor of a general testamentary power of appointment may control the disposition of the property after his death as fully as the owner of a simple title, such powers are taxed in the same manner as outright ownership."

Judge Harris in his dissent in the Ninth Circuit expressly articulated the problem of retrospectivity that the majority decision created:

> "The Congress, in the Tax Reform Act of 1976, acted to override the *Keinath* rule, but only prospectively. The effect of the decision of the majority is to give to the 1976 Amendments the retrospective effect which the Congress expressly rejected." (A-6)[8]

By refusing to apply the *Keinath* rule to a pre-1977 trust, the Ninth Circuit contravened the Congressional intent that its amendment of the law in response to *Keinath* be applied prospectively only.

H. If Treasury Regulation §25.2511-1(c) Is To Be Interpreted As The Commissioner Now Urges, Its Retroactive Application To Holders Of Interests Created Prior To The Promulgation Of The Regulation Would Be Manifestly Unfair.

Until the promulgation of Treasury Regulation §25.2511-1(c) in 1958, the rule of *Brown v. Routzahn, supra*, was universally accepted, apparently even by the Commissioner. Accordingly, in reliance on *Brown*, the holder of a

[8] The new Code section provides that a "qualified disclaimer must be made within "9 months after the later of —

(A) the date on which the *transfer creating the interest* in [the disclaimant] is made, or

(b) the day on which [the disclaimant] attains age 21." (emphasis added). I.R.C. §2518 (b)(2).

A question exists as to whether "transfer creating the interest" would include a transfer creating a contingent remainder interest. Certain of the legislative history suggests to Petitioners that is does not, but that question is not before the Court. To the extent Congress may have changed the *Keinath* rule, it clearly did so prospectively only.

contingent remainder interest, such as Jewett, had no reason to disclaim his interest prior to the death of the life beneficiary (provided that such interest could still be effectively disclaimed under the governing state law).

In 1958, Treasury Regulation §25.2511-1(c) was adopted. It applied equally to disclaimers of "transfers" occurring before and after its promulgation, and it made no provision for any grace period following its enactment within which "transfers" made by instruments predating 1958 could effectively be disclaimed. Therefore, if the Regulation is to be interpreted as the Commissioner now urges, as effecting a material change from prior law, there was never a time after the proposed and final Regulations were issued at which Jewett could effectively disclaim. Under the Commissioner's view, the "reasonable time" period for Jewett's disclaimer had commenced to run at the Testatrix's death in 1939. Twenty years later, when the Regulation was promulgated in 1958, it was already far too late for Jewett to act.

Clearly, such a result would be contrary to any reasonable notion of equity or ordered justice. Holders of pre-1958 interests should not have been arbitrarily, capriciously and suddenly deprived of their existing right to refuse to accept ownership of property without the imposition of a tax.

As discussed above, resolution of the instant case turns on the meaning of the words "reasonable time after knowledge of the existence of the transfer," as that language is used in Treasury Regulation §25.2511-1(c). Since until the promulgation of that Regulation the rule of *Brown* v. *Routzahn* had been universally accepted, it would not have been unwarranted for taxpayers to assume that the word "transfer" in the context of the Regulation had the same meaning expressed in *Brown*, that is, an actual vesting of the property interest.

A clearly-stated change from that position would have drawn well-warranted criticism, and perhaps even legislative correction. At the least, it would have caused taxpayers to reevaluate any disclaimers which they had contemplated

making. The Commissioner made no such frontal attack on existing law in 1958. Rather, over fourteen years later, through his questionable interpretation of the Regulation, he appears to be making a belated attempt to legislate a change in this policy without an unambiguous articulation of the change. *Cf. Stubbs, Overbeck & Associates, Inc.* v. *United States*, 445 F.2d 1142, 1147 (5th Cir. 1971) ("It would appear that perhaps the drafter of the Ruling did a bit of legislating for the convenience of the IRS. Only Congress has the power to do this."); *Investment Annuity, Inc.* v. *Blumenthal*, 442 F. Supp. 681, 692-94 (D.D.C. 1977).

Such veiled changes in existing law are not permissible. If Treasury Regulation §25.2511-1(c) really did effect a change from the prior law, its enactment was patently inequitable to holders of pre-1958 interests, and the Commissioner abused his discretion under Section 7805(b) of the Internal Revenue Code in failing to specify that the Regulation would not be applied prospectively only. *See International Business Machines Corp.* v. *United States*, 343 F.2d 914, 920-21, 923 (Ct. Cl. 1965), *cert. denied*, 82 U.S. 1028 (1966); *LeSavoy Foundation* v. *Commissioner*, 238 F.2d 589 (3rd Cir. 1956). His action should therefore have not been upheld. *Id.; Anderson, Clayton & Co.* v. *United States*, 562 F.2d 972, 981 (5th Cir. 1977).

Conclusion

For the reasons stated above, the judgment and opinion of the United States Court of Appeals for the Ninth Circuit entered in this proceeding on December 9, 1980 should be reversed and judgment entered for Petitioners.

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